

VZCZCXR05097

PP RUEHAG RUEHDF RUEHIK RUEHLZ RUEHROV

DE RUEHTC #1836/01 2760823

ZNR UUUUU ZZH

P 030823Z OCT 07

FM AMEMBASSY THE HAGUE

TO RUEHC/SECSTATE WASHDC PRIORITY 0455

INFO RUCPDOC/USDOC WASHDC

RUEATRS/DEPT OF TREASURY WASHDC

RUEHFT/AMCONSUL FRANKFURT 3791

RUCNMEM/EU MEMBER STATES COLLECTIVE

RUEHAT/AMCONSUL AMSTERDAM 3753

UNCLAS SECTION 01 OF 02 THE HAGUE 001836

SIPDIS

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STATE FOR EUR/WE (TSMTIH)

USDOC FOR 4212/USFCS/MAC/EURA/OWE/DCALVERT

TREASURY FOR IMI/OASIA/VATUKORALA

PARIS ALSO FOR OECD

STATE PLEASE PASS FEDERAL RESERVE

E.O. 12356: N/A

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SUBJECT: DUTCH 2008 BUDGET: REPAIRING THE ROOF WHILE THE SUN IS SHINING

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**¶1. (SBU) SUMMARY.** In presenting the 2008 national budget, the Netherlands' new center-left coalition government has opted for a series of measures aimed at promoting a "fairer" income distribution, while also ensuring the country's future financial sustainability. By introducing new taxes and increasing existing ones, the GONL seeks to finance needed improvements in the country's education structure and impoverished urban neighborhoods while also attempting to impose higher environmental and health standards. Coalition leaders argue that funding such efforts during a time of stable economic growth will ensure the country's future prosperity without jeopardizing its ability to finance increasing burdens related to an ageing population. While new Finance Minister (and Labor Party leader) Bos has succeeded in pushing through measures that support traditional Labor Party interests at the expense of tax payers, his more conservative coalition partners (Christian Democrats and Christian Union) will be wary of going too far given recent polling indicating a drop in public support for the new government since it took office in February. END SUMMARY.

MAINTAINING ECONOMIC GROWTH

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**¶2. (U)** On September 18, Dutch Finance Minister Wouter Bos presented to parliament a draft 2008 national budget, the first of the new center-left coalition government (Christian Democrats, Labor, and Christian Union). With estimated revenues totaling 147 billion euros (\$208 billion) and expenditures at 144 billion euros (\$204 billion), the budget forecasts a surplus of 3 billion euros (\$4 billion or 0.5 percent of GDP and up from the 0.2 percent forecasted for 2007). This will be the second successive year that the national budget has shown a surplus, which is expected to reach 1 percent of GDP by the end of 2011. However, the budget document also notes that projected budget surpluses in coming years could become deficits because of exposure to the U.S. subprime mortgage crisis.

**¶3. (U)** Under this budget, the national debt is expected to fall to 45 percent of GDP in 2008 from a projected 47 percent in 2007 and a

longer term target of less than 40 percent in 2011. The draft budget also assumes an estimated 2.5 percent GDP growth in 2008 (slightly lower than the 2.75 percent growth forecasted for 2007); a slight increase in inflation to 2 percent (up from an anticipated 1.5 percent in 2007); and unemployment decreasing further from an anticipated 4.5 percent in 2007 to 4 percent in 2008.

**¶4.** (U) Other key elements of the proposed 2008 budget include increased spending to improve general education needs (2 billion euros or \$2.8 billion), to raise labor participation (36 million euros or \$50.4 million) and to better conditions in impoverished neighborhoods (920 million euros or \$1.29 billion). These measures will largely be financed through personnel reductions and cost savings in the civil service sector, efficiencies gained by the transfer of certain financial responsibilities to the provinces, the introduction of environmental taxes, increased taxes on petroleum products and cigarettes, and an increase in the Value-Added Tax (VAT) from 19 to 20 percent in 2009.

#### PAYING FOR THE FUTURE THROUGH "FAIRER" INCOME DISTRIBUTION

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**¶5.** (U) These increases in environment and consumption taxes (valued at around 5 billion euros or \$7 billion) will largely be set off by cuts in other areas, such as lower unemployment premium payments. However, health care premiums will rise significantly for most of the population, except the chronically sick, and are expected to contribute to the lowering of the purchasing power of Dutch citizens in the short-term.

**¶6.** (U) Prime Minister Jan Peter Balkenende (Christian Democrat) and Finance Minister Bos (Labor) have publicly defended the coalition's budget plan as promoting a "fairer" income distribution and have rejected claims that they are simply pursuing a policy of reducing income inequalities. They argue that the plan will require financial sacrifices from most income groups while sparing lower income groups. They contend such measures -- boosted by continued economic growth and improvements in the education system (increased

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wages for teachers, free textbooks), a focus on the country's urban neighborhoods (poverty reduction efforts, employment incentive programs targeting women and minorities) and higher environmental and health standards -- will ultimately benefit future generations. They expect that the implementation of additional measures over the coming years will result in a 4-5 percent increase in the purchasing power of all Dutch citizens by 2011.

**¶7.** (U) The coalition government argues that the above measures are also needed to ensure the country's future financial sustainability and future budget surpluses. As elsewhere in Europe, the Netherlands is faced with an ageing population. Additional funds will be needed to cover expected increases in government expenditures related to pension and health care costs.

#### SMALL INCREASES ON DEFENSE, SAFETY AND COUNTERTERRORISM

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**¶8.** (U) Under the draft budget, national defense spending in 2008 will increase to 8.1 billion euros (\$11.34 billion), up slightly from the 7.9 billion euros projected in 2007. As part of this total, the coalition government has agreed to spend over the next four years 250 million euros in specific operational and personnel areas and 250 million euros on crisis management operations. The parliament has agreed to an additional 100 million euros over the next two years to fund the purchase of new equipment. The GONL has also earmarked 535 million euros over the next four years to fund "unforeseen" foreign policy expenditures, which could be used to cover additional costs related to the current Dutch military deployment in Uruzgan in Afghanistan and its possible extension.

**¶9.** (U) The draft budget also includes 5.5 billion euros (\$7.76 million) to fund Ministry of Justice (MOJ) efforts, including programs aimed at reducing crime rates by preventing social derailment and tackling outbreaks of violence and crime. The GONL plans to intensify its fight against juvenile crime and repeat

offenders (specifically through school campus and tailor-made behavioral programs) and to improve rehabilitation programs for detainees and ex-detainees. An additional 9.7 million euros in 2008 (and up to 32.3 million euros in 2011) will target efforts to combat organized crime (cyber crime, financial and economic crime, and fraud) and to train new police officers. The MOJ will also set aside an extra 1.5 million euros in 2008 (which is expected to reach 7.7 million euros in 2011) to prevent the spread of radicalization. MOJ efforts in this area will focus on prevention, including the early recognition and reversal of radicalization and social polarization trends, preferably at a local level. Multidisciplinary exercises will increase readiness for possible chemical, biological, radiological, and/or nuclear attacks.

COMMENT: REPAIRING THE ROOF WHILE THE SUN IS SHINING

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19. (SBU) While the economic outcomes of the proposed budget plan remain uncertain, Finance Minister and PvdA (Labor) Party Leader Bos has clearly made his mark by pushing through measures that support traditional Labor Party social targets at the expense of tax payers. As he told the press shortly after taking up his position within the new cabinet, "you must repair the roof while the sun is shining." His more conservative coalition partners (Christian Democrats and Christian Union) may have accepted the heavier taxation in exchange for promises of a healthy budget surplus by 2011, which coincides with the end of the current cabinet's term. However, they are also acutely aware of recent polling indicating that public confidence in the new coalition government has plummeted since it took office in February and will be cautious about allowing such trends to continue. Meanwhile, the draft budget plan is drawing criticism from both the left and the right, with the opposition conservative-liberal VVD party claiming the "hard-working" Dutch public will be hardest hit by the proposed tax increases and the opposition Social Democrats contending the coalition government's plan is still doing too little for the country's poor.

GALLAGHER